

## **Something Old and Something New Solve the Mold Insurance Problem In Commercial Construction**

**By David J Dybdahl, CPCU, ARM,**

The introduction of universal mold related claims exclusions in commercial, residential and professional liability insurance policies have left everyone involved with construction projects virtually uninsured for mold related damages. Developers, contractors, owners and their lenders no longer have insurance protection in their traditional insurance programs for most liability or property losses in anyway related to mold.

The need for prospective insurance on mold related damages is expected to increase dramatically as all of the parties involved in the construction of new buildings come to grips with the long ranging risk management implications of universal mold exclusions in property and liability insurance policies.

Anticipating the need for mold insurance products, a small team of building scientists and environmental insurance experts began work in 2001 on an insurance policy designed to help manage the environmental and water intrusion loss exposures of commercial construction projects. The revolutionary insurance product designed specifically for this purpose is called Real Estate Environmental Liability insurance with Highly Protected Risk coverage for Mold. (REEL/HPR/Mold) To develop this insurance product the design team married two loss control engineering concepts that were developed one hundred years apart, HPR loss control engineering and Building Science.

### **Putting Mold Risks Into Perspective**

The Insurance Information Institute estimates that mold losses cost insurance companies three billion dollars in 2002. In addition to these losses, personal injury claims for mold related injuries could be at least this high. To put these loss figures into perspective, fire losses were about twelve billion dollars in the same year. The big difference between mold losses and fire losses from a risk management perspective is fire losses are universally insured today in standard insurance programs, mold related losses universally are not.

With mold related losses equaling approximately one out of every four fire claims, being completely uninsured for mold in new construction projects is not likely to be a long-term option for the parties involved with new construction or anyone owning property occupied by humans. Eventually the project finance community

will figure out the insurance industry has dumped billions of uninsured mold related losses back into the economy with the successful introduction of universal mold exclusions in virtually all insurance policies sold today. Without prospective insurance, project financing could dry up as lenders and financial rating organizations come to grips with collateral that is virtually uninsured for mold related damages and firms that are now completely uninsured for the potential toxic tort liabilities associated with mold.

### **Something Old**

Insurance companies have long known it is less expensive to prevent a loss than to pay for one after it has occurred. This is especially evident in Boiler and Machinery insurance where many years ago insurance companies created specialized engineering capabilities to inspect boilers to identify problems before a boiler exploded and took the building and the occupants with it. By prefunding loss control services into the insurance premium, insurers were able to avoid incurring large losses under their policies which gave the insurer offering engineering services a competitive advantage over insurance companies who merely paid for losses after they were incurred. Giving premium credits to buildings with sprinklers is another example of insurance companies financing loss control protocols to create a competitive advantage. Over time the insurance products sold to these highly engineered risks became known and marketed as Highly Protected Risk (HPR) insurance policies. These same HPR engineering concepts were utilized to develop the REEL/HPR/Mold insurance product for new construction.

### **Something New**

Anticipating there would be new demand for prospective insurance covering the mold hazard, a small insurance product development team at American Risk Management Resources Network, LLC and mSolve, LLC. started in 2001 to create an insurance product would provide good coverage and was affordable. The research team found the answer to predicting and controlling loss exposure in the relatively new field of Building Science. Building Scientists study the relationships between the air, heat and moisture flows in a building and how they may impact building performance. Through these techniques they are able to identify incompatible dynamics of building designs, building materials and construction practices to avoid problems that may cause building failures.

Research into the root causes of mold related losses in the United States revealed that the relative risk of a building can vary as much as by 5000% depending on the building envelope design, building materials, HVAC designs, building codes, code enforcement, the quality of the craftsmanship and the region the building is located in.

Contrary to popular belief, climate is not a good predictor of mold risk. In the relative hazard ranking model developed to support the insurance REEL/HPR/Mold underwriting process, the desert states Nevada and Arizona made it to the top ten list of high hazard states and Louisiana did not even make it to honorable mention. It will be no surprise to most readers that Texas has the highest loss frequency rate in the United State. Wisconsin has the lowest relative mold loss rate, which is one-fiftieth the failure rate in Texas based on the relative frequency of insurance claims.

Integrating Building Science expertise into a prefunded HPR insurance product was the key to providing a insurance coverage period long enough to get the contractor and developer past the statute of repose. The building scientists are able to identify problematic designs, monitor the construction process and provide on going loss control services over the course of the policy term to avoid mold related losses through the proper operation and maintenance of the building.

### **REEL/HPR/Mold Insurance**

After three years of research and development the REEL/HPR/Mold insurance product emerged from the insurance product design team. The REEL/HPR/Mold product is the only environmental insurance product designed to insure all the environmental hazards of new construction including preexisting site conditions and to provide prefunded building science based loss control services.

There are a number of unique features in the REEL/HPR/Mold insurance product. First the policy cannot be cancelled so once it is purchased the Developer, General Contractor and Lender are assured of continued insurance protection for the entire length of the multi-year policy term. Upon the sale of the building the Owner can be assigned the policy without additional premium while the original named insured parties stay on the policy as Additional Named Insureds. When the policy is assigned, the owner becomes the first named insured and assumes responsibility for the deductible. The new owner also commits to providing access to the building for the Building Science loss control engineers, which creates a managed risk for the developer and contractor even after they have relinquished control of the building to the owner. Also unique to this insurance product, Building Science based loss control is paid for by the insurance company as part of the insurance premium beginning in the design phase and over the entire policy period.

The REEL/HPR/Mold policy provides liability insurance for Bodily Injury, Property Damage, Clean Up and Defense for claims arising out of the release of Pollutants including Mold/Fungus at the insured location. The policy features no-fault on site clean up coverage of regulated hazardous materials. This single policy is designed to fill the gaps in business insurance coverage's for all of the principal parties associated with a new commercial construction project.

Mold losses measured in the tens of millions of dollars are fairly common with some claims measured in the billions of dollars making it to the press. Therefore the REEL/HPR/Mold product is offered with limits up to \$25,000,000. Policy terms of up to ten years are available.

The rates charged for a REEL/HPR/Mold policy range from \$.70 - \$2.00 per square foot for a \$10,000,000 limit and a 10-year policy term. Rates vary depending on sixteen different rating variables. A single premium covers the entire policy term. The minimum premium for a 10-year policy is \$100,000. Lower limit and coverage term options are also available.

## **Conclusion**

Being completely uninsured for mold related losses in new construction projects will not be a long term option for the businesses involved with commercial construction. The REEL/HPR/Mold product is available to fix the insurance coverage gaps for the developer, general contractor, and owner. Developed through a marriage of the 100-year old loss control engineering concept of Highly Protected Risk and the new engineering specialty of Building Science, the prefunded loss control services in the REEL/HPR/Mold create a managed environmental/mold risk for the entire statute of repose period in most states.

## **Available in the US and Canada through American Risk Management Resources Network, LLC,**

The REEL/HPR/Mold insurance product was developed by American Risk Management Resources Network, LLC. in cooperation with mSolve,LLC. All inquiries for this limited distribution insurance product should be directed to the closest ARMN.Network office @ [www.armr.net](http://www.armr.net) or to David J. Dybdahl, CPCU, ARM at [Dybdahl@armr.net](mailto:Dybdahl@armr.net), 608 836 9590. For information on the building science loss control support for the REEL/HPR/Mold product contact Ed Carroll at [ecarroll@msolvellc.com](mailto:ecarroll@msolvellc.com), 608 663 4735